

ORIGINAL

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Review of Florida Power Corporation's Earnings, Including Effects Of Proposed Acquisition of Florida Power Corporation by Carolina Power & Light

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CONFIDENTIAL
REBUTTAL TESTIMONY
OF
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ON BEHALF OF
FLORIDA POWER CORPORATION

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1 mutual sharing. In other words, all stakeholders are much better off if
2 neither side benefits at the expense of the other, and both sides benefit
3 from their joint relationship. That is precisely what the FPC regulatory
4 plan seeks to accomplish. Shareholders recover the costs of completing
5 the merger to the extent that synergy savings are sufficient to cover the
6 expense. Furthermore, FPC has strong incentives to beat this spread.
7 Regardless, customers are guaranteed an immediate and recurring \$5
8 million retail rate credit for 15 years. Because savings are greater than
9 the amount of the transaction and transition costs, both sides are better
10 off; a classic win-win situation based on "splitting the savings."

11 **Q. AT PAGE 23 OF HER DIRECT TESTIMONY, MS. DISMUKES ASSERTS**
12 **THAT OF THE \$175 MILLION IN PROJECTED**
13 **SYNERGY SAVINGS ARE ATTRIBUTABLE TO PROGRESS**
14 **ENERGY'S NONREGULATED AFFILIATES. PLEASE RESPOND TO**
15 **HER ASSERTIONS.**

16 **A.** It is not clear from Ms. Dismukes' testimony if she disputes or agrees with
17 her own breakdown of the synergies attributable to Progress Energy's
18 nonregulated operations. She is clear in her observation that FPC is
19 getting the smallest share of synergies. However, she does not dispute
20 Mr. Myers' testimony with respect to the way the synergy breakdown and
21 allocation was developed. Further, Ms. Dismukes fails to recall that the
22 percentage of the transaction costs that FPC seeks to recover from these
23 savings is exactly equal to the percentage of synergies it expects to

1 receive. In other words, if FPC is under represented on the savings side,
2 it would similarly be under allocated on the transaction cost side. Ms.
3 Dismukes does speculate that "it is possible that the premium paid for
4 FPC's stock relates to the enhanced potential for profits from future
5 unregulated operations." This is, to some extent, undoubtedly true. And it
6 is also true that these same unregulated enterprises will be assigned the
7 responsibility of the transaction costs.

8 **Q. AT PAGES 24-25 OF HER DIRECT TESTOMONY, MS. DISMUKES**
9 **STATES THAT IN ONLY ONE OF THE STATE ORDERS THAT YOU**
10 **ATTACHED AS EXHIBIT CJC-2 DID THE COMMISSION PERMIT THE**
11 **RECOVERY OF AN ACQUISITION PREMIUM. PLEASE RESPOND TO**
12 **HER ASSERTION.**

13 A. Ms. Dismukes is simply setting up a convenient straw person to knock
14 down. Her entire discussion of acquisition premium recovery in other
15 jurisdictions is misguided and irrelevant. First, I must point out that I
16 offered Exhibit CJC-2 to show examples of states in which the respective
17 state Commissions had followed a front-end loading transaction cost
18 recovery principle in designing their regulatory plans to share merger
19 savings. As can be seen from reviewing CJC-2, in most of these cases
20 the Commission allowed the merging utility to keep a portion of (i.e.,
21 share) the merger savings to pay for the transaction costs associated with
22 the merger. Thus, most of these regulatory commissions recognized the
23 need to allow merging utilities the opportunity to recover their transaction

1 the state of deregulation in the industry, I think that it is very uncertain
2 when, or even if, deregulation will actually occur at the retail level.
3 Certainly, the California experience has put a damper on retail
4 deregulation initiatives across the country. Furthermore, deregulation is
5 not a precise concept. Most now realize that the "devil is in the details" of
6 any deregulation transition plan.

7 **Q. AT PAGE 13 OF HER DIRECT TESTIONY, MS. BROWN STATES THAT**
8 **THE EXECUTIVE SEVERANCE PAYMENTS WERE NOT**
9 **REASONABLE. DO YOU AGREE?**

10 A. No. It is customary for valuable and key executives to have in place
11 change in control provisions in their contracts that pay them multiples of
12 their annual salaries if they lose their positions through a merger. Without
13 such provisions, executives would demand higher current compensation
14 and would be loath to explore merger opportunities that might cause them
15 to lose their position. Consequently, with such provisions in place, key
16 executives are encouraged to seek out and complete mergers that will
17 benefit shareholders and customers. Consequently, I disagree with Ms.
18 Brown that these transition expenses are unreasonable. To the contrary,
19 these are reasonable and necessary costs, without which this merger and
20 other beneficial mergers would likely not occur.

21 **Q. AT PAGES 13-14 OF HER DIRECT TESTIMONY, MS. BROWN**
22 **ARGUES THAT THE ALLOCATION OF MERGER SYNERGIES**
23 **SHOULD REFLECT**

1 ACCRUE TO SHAREHOLDERS.

2 DO YOU CONCUR WITH HER STATEMENT?

3 A. No. First, that Ms. Brown asserts accrues to
4 shareholders reflect the fact that income taxes capture 38.575% of gross
5 synergy. Second, these after-tax cost saving synergies are being used to
6 pay the transaction and transition costs associated with the merger.
7 These are costs that have been incurred. The key to understanding
8 FPC's proposed regulatory plan is to focus on the net synergy savings,
9 those savings that remain after paying all the costs necessary to secure
10 the savings. FPC's customers are guaranteed an annual \$5 million rate
11 credit, and have additional opportunities to receive even greater savings
12 under the ESM that I recommended in my Direct Testimony.

13 Q. AT PAGE 14 OF HER DIRECT TESTIMONY, MS. BROWN ALSO
14 SUGGESTS THAT ARE
15 SUPPORTED BY THE PRODUCTION FUNCTION AND THAT
16 ADDITIONAL TRANSACTION AND TRANSITION COSTS SHOULD BE
17 ALLOCATED TO THE SHAREHOLDERS TO RECOGNIZE THIS
18 SUPPORT. SHE FURTHER ASSERTS THAT SHARED SERVICES
19 SUPPORTS THE PRODUCTION FUNCTION, MEANING THAT
20 ADDITIONAL TRANSACTION AND TRANSITION COSTS SHOULD BE
21 ASSIGNED TO THIS FUNCTION. PLEASE COMMENT.

22 A. I disagree with Ms. Brown. FPC personnel have gone to great lengths to
23 fairly allocate the synergies to the business units where the savings will